October 1989 Monthly Survey November 8, 1989

Surveys of Consumers

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The Confident Consumer

Slight Decline in Index Following Strong Gain

The Index of Consumer Sentiment was 93.9 in the October 1989 survey, down from 95.8 in September. The small October decline of 1.9 Index-points was not surprising following the 6.2 Index-point gain recorded in September. Overall, the October 1989 reading was above the third quarter average of 92.5 and nearly equal to the year earlier reading of 94.1.

Among families with incomes of $40,000 or more, the Index of Consumer Sentiment was 103.6 in October, slightly ahead of the 103.0 recorded in September, and nearly identical with the 103.7 recorded in October 1988.

Confidence Perseveres at High Levels Throughout Long Expansion

Since the cyclical peak was reached at the start of 1984, the Index of Consumer Sentiment has averaged 93.9, with the October 1989 survey equal to that average. Moveover, the Index has shown relatively small quarter-to-quarter variations throughout this period. From the first quarter of 1984 through the third quarter of 1989 the Index ranged between 99.5 and 90.5, except for the fourth quarter of 1987 when the stock market crash temporarily depressed the Index to 86.4.

This remarkable record is in sharp contrast to the decade of the 1970s, when the Index never exceeded the average recorded during the last five years, and was dominated by wide swings rather than the present stability.

Attitude trends during the current expansion are more comparable to those recorded during the 1960s. Although the 1960s are remembered mainly for the robust expansion in the first half of the decade, during the mid 1960s, as now, the economy experienced a significant slowdown in economic growth. And then as now, changing credit conditions play a key role in shaping consumer behavior.

While the prolonged maintenance of consumer confidence at high levels is certainly a welcome development, that consumer confidence has remained relatively unchanged for so long has diminished its stimulative impact on spending behavior. The most stimulative impact stems from repeated and cumulative improvements in consumer attitudes and expectations. While the maintenance of attitudes at high levels in no way augurs a recessionary decline in spending, neither does it provide the support for continued increases.

Consumer spending during the year ahead will continue to provide an underlying source of strength for the economy. Sales of homes and vehicles, however, will continue to be sluggish, with unit sales falling slightly below the year earlier levels. Interest rate developments will play an important role in shaping the timing and determining the extent of these purchases.

Friday the 13th:
Quickly Dismissed

The steep plunge in stock market prices recorded on October 13th had a significant, but short-lived, impact on consumer expectations. Interviews conducted from Friday the 13th to Monday the 16th reflected the news of the steep market plunge. The Index of Consumer Sentiment dropped sharply during that weekend, but quickly rebounded during the following week. Like the plunge in stock market prices in 1987, the entire concern was focused on prospects for the general economy, not on personal finances.

Leading Indicator
Maintained At Elevated Level

The Index of Consumer Expectations was 87.2 in the October 1989 survey. Although this was somewhat below the 88.6 recorded in September, most of the strong gain from the 80.3 recorded in August was maintained in October. The overall trend remained positive, with the October reading above the third quarter 1989 average of 84.8 and slightly above the 87.0 recorded in October 1988.

Personal Financial
Prospects Viewed Favorably

Among all families in the October 1989 survey, 42 percent reported that their financial situation had improved, unchanged from the figures recorded one month and one year earlier. Income increases were reported by 32 percent of all families, just below the 34 percent recorded one year earlier. Offsetting this small decline, complaints about the rising cost of living fell to 11 percent in October 1989 from 15 percent one year earlier.

American families remained very upbeat about prospects for their financial situation during the year ahead. In the October 1989 survey, 41 percent expected their financial situation to improve during the year ahead, up from 38 percent one month earlier and 36 percent one year earlier. Just 7 percent of all families expected their financial situation to worsen during the year ahead, down from 9 percent in September and 12 percent in October 1988. Overall, this was the best outlook for personal finances recorded in more than a year.

Outlook for Economy
Remains Positive

The October 1989 survey recorded little change in consumers' assessments of the current state of the national economy or in the direction of change that was expected during the year ahead. Overall, consumers continue to expect the economy to follow its recent path of slow growth during the year ahead.

Among all families, 47 percent in the October survey thought that the economy had improved, just between the 48 percent recorded one month earlier and the 46 percent recorded one year earlier. With regard to the year ahead, the majority of consumers in the October survey expected the performance of the national economy to remain unchanged (61 percent). The performance of the national economy was expected to improve by 22 percent, while 15 percent expected worsening conditions--both figures were within one percentage point of the month and year earlier readings.

The expected continuation of the economic expansion meant that the majority anticipated good times financially. For the economy as a whole, good times financially were expected by 53 percent of all families in the October 1989 survey, just below the 55 percent recorded one month earlier and the 54 percent recorded one year earlier.

Longer term prospects for the economy, however, did weaken to a somewhat greater extent than the outlook for the year ahead. Among all families, 36 percent expected good times financially during the next five year in the October survey, down from 41 percent in September and 40 percent in October 1988.

The positive short term outlook was supported by favorable employment expectations. The majority of families in the October 1989 survey (55 percent) expected the national unemployment rate to remain unchanged at its current low level during the year ahead. Among the other half of consumers, however, more expected the unemployment rate to increase than to decline by nearly a two-to-one margin (30 versus 14 percent). Interestingly, the proportion that expected declines as well as the proportion that expected increases in unemployment both edged upward in October. The proportion of families that expected a declining unemployment rate rose to 14 percent in October from 11 percent a month earlier, while the proportion that expected an increasing unemployment rate rose to 30 from 26 percent.

Inflation Expectations

The annual rate of inflation expected by consumers was 4.7% in the October 1989 survey. This represents a return to the level recorded in the August survey, following the decline to 4.4% in September. Despite this small uptick, the overall trend remains downward: the October 1989 reading is still below any of the monthly readings in the first half of 1989, and below the 5.2% recorded a year earlier.

Interest rates were expected to increase by 55 percent of all families in the October 1989 survey, up from 50 percent in September, but well below the peak of 75 percent recorded in April 1989 and the 68 percent recorded last October.

Favorable Price Perceptions Support Home Buying Attitudes

The proportion of families holding favorable attitudes toward buying conditions for homes was 66 percent in the October 1989 survey. Although this was below the 70 percent recorded in September, it was the second highest figure recorded during 1989, and above the 64 percent recorded in October 1988.

The recent strength in home buying attitudes has been due to favorable perceptions of home prices; this strength, however, has been offset by rising mortgage interest rates. Overall, home buying attitudes remain favorable, but are now substantially below the cyclical peak of 86 percent recorded in 1986. This was due almost entirely to concerns about rising mortgage interest rates.

Perceptions of home prices are very favorable. Among all families in the October 1989 survey, 26 percent mentioned the availability of good buys on homes, just ahead of the 25 percent recorded one month earlier and significantly above the 18 percent one year earlier. To put this in perspective, the highest proportion to favorably mention home prices during the last thirty years was 27 percent--recorded in both 1986 and 1988.

The small October decline in favorable home buying attitudes (as well as the larger decline from the cyclical peak) has been due to less favorable perceptions of mortgage interest rates. Among all families in the October 1989 survey, 29 percent mentioned the current availability of low mortgage interest rates, down from 36 percent in September. In comparison, when the 1986 peak was reached in favorable home buying attitudes, 78 percent cited the appeal of low mortgage interest rates.

Vehicle Buying Attitudes Remain On Favorable Plateau

Favorable attitudes toward buying conditions for vehicles were held by 62 percent of all families in the October 1989 survey, just ahead of the 61 percent recorded in the prior two months and the 60 percent recorded in October 1988. Attitudes toward vehicle buying conditions have remained remarkably stable, with the last 20 monthly surveys recording a figure between 60 and 65 percent (with 14 of these reading either 61 or 62 percent!)

The availability of price discounts and rebates was reported by 36 percent of all families in the October 1989 survey, up from 32 percent one

month earlier and 31 percent one year earlier. At 36 percent, the October 1989 reading was the highest in two years, and only marginally below the all-time peak of 38 percent recorded in 1975.

Because of the continuous use of these price discount programs, however, consumers have come to expect their availability, and thus their impact on overall buying attitudes has diminished. Moreover, the impact on consumer attitudes is now asymmetrical: the availability of discounts is taken for granted; their absence is met with postponement of purchases. As a result, consumers have now come to view price discount programs as simply a means to determine the timing of their purchases, shifting purchases from one month to the next depending on their availability.

Although attitudes have remained stable at this relatively high plateau, it is certainly well below the 1986 cyclical peak of 81 percent. That cyclical peak was induced by the availability of interest rate discounts on new vehicle purchases at the end of the 1986 model year. It is the availability of these interest rate discounts, especially on longer term loans, that many fewer consumers report in the current surveys.

The proportion that mentioned the availability of discounted interest rates fell to 13 percent in October from 18 percent one month earlier and 25 percent six months earlier (the 1989 high). In comparison, at the 1986 peak in vehicle buying attitudes, a record 70 percent supported their favorable buying attitudes by mentioning the availability of interest rate discounts.

Household Durables

Consumers' assessments of buying conditions for appliances, furniture, and home electronic goods remained at favorable levels in the recent survey. Favorable buying attitudes were held by 73 percent of all families in the October 1989 survey, down from 75 percent in September, but equal to the October 1988 reading. Buying conditions for household durables were viewed favorably because of the continued widespread availability of price discounts. Mentions of price discounts were made by 35 percent of all families in the October 1989 survey, just above the 34 percent recorded one month earlier and the 32 percent recorded one year earlier.

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The October 1989 survey included 500 completed interviews conducted between October 2 and October 29, 1989.